

**BUCKNELL STEHLIK SATO & STUBNER, LLP**  
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JUDGE: Philip H. Brandt  
DATE: October 28, 2008  
TIME: n/a  
CHAPTER: 11  
LOCATION: Seattle  
RESPONSE DATE: October 20, 2008

4

5

UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF WASHINGTON, AT SEATTLE

22           1. My name is Jerry N. Stehlik. I am a partner in the firm of Bucknell Stehlik Sato &  
23 Stubner, LLP, located in Seattle, Washington. My firm is counsel for the plaintiffs in this adversary  
24 proceeding. I provide this declaration to demonstrate to the court the extent and subject matter of

26

27

28 Declaration of Jerry N. Stehlik - 1

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1 discovery and other related matters that have been occurring in the underlying Chapter 11 case  
 2 involving the plaintiffs and the defendant in this adversary proceeding, who are the debtors and  
 3 subordinated secured creditor, respectively, in the Chapter 11 case.

4       2. The defendant in this case has conducted extensive discovery in the related Chapter  
 5 11 case. Ostensibly, this discovery is related to two contested motions that the debtors had filed in  
 6 the bankruptcy case, one is the debtors' motion for post-petition financing, and the other is a motion  
 7 by the debtor Redmond 74, Inc. to approve a sale of property free and clear of liens to Velo  
 8 Redmond, LLC. On September 30, 2008 defendant served an extensive set of interrogatories and  
 9 requests for production on the debtors. The defendant also subpoenaed financial and lending records  
 10 from the debtor. The debtor produced over 35,000 pages in response to these discovery requests.  
 11  
 12 On October 14, 2008, defendant took the deposition of two witnesses, one was Daryl Stromswold, a  
 13 financial officer for the debtors, and the other was Robert Pascal, a vice president of HomeStreet  
 14 Bank. Again, HomeStreet Bank is the primary secured lender to the debtors and the lender which is  
 15 providing post-petition financing to the debtors. Referenced deposition pages are attached and  
 16 incorporated herein.  
 17  
 18

19       3. The deposition of Mr. Stromswold generated a transcript of 147 pages. The topics  
 20 covered in that deposition included: the relationship between Redmond 74 and Brian Housley, a  
 21 principal in Velo Redmond, LLC, the contract purchaser of the 19 lots or "units" to which defendant  
 22 has objected (Stromswold Dep. at P. 98-101), a description of the documents produced by the  
 23 debtors consisting of all documents related to negotiations with the bank (HomeStreet) and all other  
 24 lenders they have talked to and private investors from 2007 through the present, consisting of over  
 25  
 26

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Declaration of Jerry N. Stehlak - 2

1 35,000 pages of documents (Stromswold Dep. at p.29 and 141); questions relating to the debtors  
 2 relationship with HomeStreet Bank, and in particular whether or not the debtors were ever in default  
 3 with HomeStreet Bank (Stromswold Dep. at p.51); discussion of counsel as to the appropriate scope  
 4 of the deposition as between Chapter 11 and adversary issues wherein counsel for the defendant  
 5 stated: "I'll tell you what, there is a little overlap, no denying it." (Stromswold Dep. at p.62); the  
 6 position taken by the defendant in opposition to the proposed sale of lots by Redmond 74, Inc.  
 7 (Stromswold Dep. at p.90, 106 and 126); and a discussion of the proposed sale to Velo Redmond,  
 8 LLC (Stromswold Dep. at p.116). As discussed in plaintiffs' Opposition Memorandum, defendant's  
 9 refusal to release its lien rights to allow the sale of lots by Redmond 74, Inc. to Velo Redmond, LLC  
 10 is directly at issue in this adversary proceeding. The defendant has characterized this proposed sale  
 11 as a "sham" both in its motion and in the Answer and Counterclaims filed in this adversary  
 12 proceeding. Unquestionably, the defendant attempted to and succeeded in conducting discovery on  
 13 this issue in the course of the Stromswold deposition.

14       4.      The Robert Pascal deposition generated a transcript of 94 pages. This deposition  
 15 extensively explored the lending relationship by and between the debtors and HomeStreet Bank and  
 16 in a number of places touched on issues in the adversary proceeding. For example, Mr. Pascal  
 17 discussed the structure of the financing that was put in place to facilitate the sale of Redmond 74,  
 18 Inc. property which was thwarted by defendant's refusal to release its lien (Pascal Dep. at p.65 and  
 19 66). He also discussed the need of Redmond 74, Inc. to file a bankruptcy proceeding to force  
 20 defendant to subordinate its lien position to permit construction financing to Little Boat by  
 21 HomeStreet Bank (Pascal Dep. at p.75). Mr. Pascal also addressed whether the debtors were in  
 22

23       HomeStreet Bank (Pascal Dep. at p.75). Mr. Pascal also addressed whether the debtors were in  
 24  
 25  
 26  
 27  
 28     Declaration of Jerry N. Stehlik - 3

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1 default in loans with HomeStreet Bank and whether HomeStreet Bank declared a default (Pascal  
 2 Dep. at p.11). The subject matter covered in Mr. Pascal's deposition relates to several issues in this  
 3 adversary proceeding, including the plaintiffs' claims that the defendant wrongfully refused to  
 4 subordinate its lien position to allow the sale of Redmond 74, Inc. lots and defendant's justification  
 5 for doing so based upon the alleged default by the plaintiffs under the HomeStreet Bank loans.  
 6 Defendant alleges in paragraph 3.6 of its counterclaim that "The Rainier Acquisition Financing  
 7 provided that a default under HomeStreet's A&D Loan was also a default on the Rainier Acquisition  
 8 Financing", and later in paragraph 3.20 asserted that this "default" justified its refusal to subordinate  
 9 to proposed construction loans by HomeStreet Bank to Little Boat. Here again, by conducting dis-  
 10 covery for the ostensible purpose of opposing debtors' motion to approve post-petition financing in  
 11 12 the Chapter 11 case defendant has waded into issues in this adversary proceeding.  
 13

14 5. In addition to requesting and seeking documents from the debtors, the defendant also  
 15 subpoenaed records from HomeStreet Bank. That subpoena sought "complete copies of all loan  
 16 write-ups, collateral analysis, correspondence and internal memoranda, regarding any loan made by  
 17 HomeStreet Bank to, or requested by: Little Boat North, Inc., Redmond 74, Inc., Robert Baldwin,  
 18 Garth Schlemlein, Mark Dean, Will Fernyhough, or any business entity owned or controlled by any  
 19 of those persons." Here again, the lending relationship between the plaintiffs, the defendant and  
 20 HomeStreet Bank are deeply intertwined and the issues upon which the defendants have already  
 21 conducted substantial discovery in the bankruptcy case also touch upon directly and indirectly a  
 22 number of the issues in this adversary proceeding.  
 23

24 //

25

26

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28 Declaration of Jerry N. Stehlik - 4

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1 I declare under penalty of perjury that the foregoing is true and correct.  
2

3 DATED this 20<sup>th</sup> day of October, 2008.  
4



Jerry N. Stehlik

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28 Declaration of Jerry N. Stehlik - 5

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Daryl L. Stromswold

Page 1

1                   UNITED STATES BANKRUPTCY COURT  
2                   WESTERN DISTRICT OF WASHINGTON

3       In re    )  
4    )  
5       LITTLE BOAT NORTH, INC.                                      )  
6       7525 SE 24th STREET, #650                                      )  
7       MERCER ISLAND, WA 98040,                                      )  
8       Tax ID 20-3046005,    )  
9    )  
10   )  
11    )  
12    )  
13    )  
14    )  
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16    )  
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19    )  
20    )  
21    )  
22    )  
23    )  
24       DATE TAKEN: OCTOBER 14, 2008  
25       REPORTED BY: SHERRILYN SMITH, CCR# 2097

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Daryl L. Stromswold

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1 Q And, in fact, there were a series of  
2 applications made in 2008, right?

3 A There's a series of ongoing negotiations with  
4 the bank, yes.

5 Q And also a series of ongoing negotiations  
6 with potential replacement subordinate capital for  
7 Redmond 74, right?

8 A Yes.

9 Q Were all of those documents produced as part  
10 of the bankruptcy filing, to your knowledge, or just  
11 the ultimate last set?

12 MR. KORNFELD: I'm going to object.  
13 When you say "bankruptcy filing," ambiguous. Are we  
14 talking about things filed in the bankruptcy court?  
15 Are we talking about the documents that we produced  
16 to you last night?

17 MR. WEATHERHEAD: I guess I don't know.  
18 I'll ask that question, too.

19 MR. KORNFELD: More for clarity than  
20 anything else.

21 A To the best of my knowledge, all the  
22 documents we produced to you last night include all  
23 the negotiations with the bank and the subordinated  
24 debt with lenders we've talked to, the private  
25 investors, from late 2007 through now.

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1           Go ahead.

2           Q   Did you have any idea why HomeStreet Bank was  
3 asking you for that?

4           A   It's not unusual for us to give them  
5 corporate cash flows or discuss our corporate cash  
6 flows with the bank.

7           Q   And HomeStreet Bank is a lender to --

8           A   Yes.

9           Q   To whom?

10          A   HomeStreet Bank is a lender to Little Boat  
11 North, Redmond 74, TDC, Falling Water, 305 Lakeside  
12 and the founders. That's all that comes to mind, off  
13 the top of my head.

14          Q   And was it your understanding that the  
15 request you received from Mr. Pascal for information  
16 was in connection with those loans?

17          A   It's in relationship with the ongoing  
18 relationship with the bank, yes.

19          Q   Are any of the loans that you just identified  
20 in default, to your knowledge?

21          A   I have not received any notices of default.

22          Q   I guess my question is: Are any of them in  
23 default, whether or not you have been notified of a  
24 default by the bank, to your knowledge?

25           MR. KORNFELD: Object to the extent it

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1 for the 2007 return, did you have to change any of  
2 the assumptions about allocation of cost and overhead  
3 to the Bennett sale?

4 A We reviewed the cost and assumptions and  
5 estimates in making the final determinations --  
6 profit for the year, yes.

7 Q And how did you change them as a consequence  
8 of that review?

9 MR. KORNFELD: I'm going to object to  
10 this line of questioning. I've given you a fair  
11 amount of room, but we do have an adversarial  
12 proceeding filed. The law is pretty clear that this  
13 particular discovery mechanism is not appropriate. I  
14 think you are leading into the adversary proceeding.  
15 I'm going to ask you to move on.

16 MR. WEATHERHEAD: I'll tell you what,  
17 there's a little overlap, no denying it.

18 MR. KORNFELD: Yeah.

19 MR. WEATHERHEAD: However, you have  
20 made some representations about the value of this  
21 project and the profitability of the project is  
22 intrinsic to that value representation that you have  
23 made. I think I am entitled to inquire whether  
24 profit previously taken has now been reallocated to  
25 try to thrust it forward to enhance the value of the

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1 products that were in development when this started  
2 and they have had to come off their price points to  
3 recover their bases.

4 Q All right.

5 And what efforts have you made to sell  
6 product at Redmond 74 or Little Boat North to test  
7 whether that hypothesis holds true; that the land  
8 would stay stable or whether this is one where you  
9 would have to move off your price point?

10 A We have not.

11 Q Not at all?

12 A We cannot because there is no place for  
13 vertical construction at Redmond 74. We cannot  
14 obtain financing without the subordination of Rainier  
15 Capital, so we have no option to do that at Redmond  
16 74.

17 At Little Boat North we have existing  
18 inventory that we are trying to sell through and we  
19 prefer to sell through that inventory before we try  
20 this.

21 Q All right.

22 You haven't sold any inventory in Little Boat  
23 North in how long?

24 A Probably two months, it could be.

25 Q Have you adjusted your price points for

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1 Basically, an update. People were talking to  
2 concepts that were under discussion, possible  
3 strategies to sell the projects.

4 Q All right.

5 And which projects were you talking about?

6 A Redmond 74, Little Boat North, Jacobson House  
7 and Little Duck.

8 Q And then maybe you can just sort of help me  
9 out. The first one says "Stanton Northwest."

10 A Yes.

11 Q Who is Stanton Northwest?

12 A Stanton Northwest is an entity owned by  
13 Brian Housley, and his wife, I believe, is Sheila.

14 Q And how was Stanton Northwest contacted, if  
15 you know?

16 A My recollection is that Stanton Northwest was  
17 contacted through an associate of Mr. Baldwin.

18 Q Do you know who the associate was?

19 A Wayne Knowles.

20 Q And who is Wayne Knowles?

21 A Wayne Knowles is a person that's been  
22 involved in residential and commercial real estate in  
23 the Seattle marketplace for a number of years. He  
24 has had prior business dealings with Mr. Baldwin.  
25 That's all I know.

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1 Q So is it your understanding that Mr. Baldwin  
2 mentioned to Mr. Knowles that he was on the lookout  
3 for potential investors and that Mr. Knowles directed  
4 him to Mr. Housley?

5 A That would be my assumption, yes.

6 Q And prior to this reference, or this  
7 referral, I should say, by Mr. Knowles, do you know  
8 whether Mr. Housley or any of his entities had any  
9 connection with Mr. Baldwin or any of his entities?

10 THE WITNESS: Can I tell him?

11 MR. KORNFELD: Yes.

12 A I'm not aware of any relationship between  
13 Urban Innovations and Stanton Northwest. Mr. Baldwin  
14 has stated on a number of occasions that prior to  
15 Mr. Knowles making the introduction, he had no  
16 relationship with Brian Housley.

17 Q Okay.

18 And did you have any relationship with Brian  
19 Housley?

20 A No.

21 Q Ever heard of him before Mr. Knowles referred  
22 to him?

23 A No.

24 Q All right.

25 Were you privy to any of the discussions

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1 between Mr. Baldwin and Mr. Housley?

2 A Yes.

3 Q And what was discussed?

4 A The acquisition of Little Boat North,  
5 Jacobson House and Redmond 74 by Mr. Housley or one  
6 of his entities.

7 Q And were there discussions about the terms on  
8 which that might take place?

9 A Yes.

10 Q Tell me about those.

11 A Basically, it was a buyout, is how we started  
12 the discussions. We wanted Mr. Housley to purchase  
13 all three entities. Mr. Housley was going to go out  
14 and arrange the debt financing for himself and  
15 acquire the properties.

16 Q And is that the way it turned out?

17 A No.

18 Q Why not?

19 A A number of factors played into it.  
20 Mr. Housley's financial capability to acquire all  
21 three projects, his ability to find the financing, he  
22 was looking for subordinated debt to help him buy the  
23 projects, and eventually we came to terms that worked  
24 for both parties.

25 Q So are you saying that he had insufficient

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Daryl L. Stromswold

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1 credit capacity himself to do the deal through the  
2 bank on his own?

3 MR. KORNFELD: I'm going to object to  
4 the extent it calls for speculation. Daryl may or  
5 may not know, obviously, his credit situation.

6 Q I'm sorry, I'm not asking you to speculate,  
7 but I thought you told me that one of the factors was  
8 that Mr. Stanton didn't have the financial oomph to  
9 do the deal on his own on the terms that you would  
10 have originally liked him to.

11 A I believe the value of all three of these  
12 projects was 35- to \$45 million of debt. When  
13 Mr. Stanton saw that number, he decided we should  
14 renegotiate something else to make this work.

15 Q So where did it go from then, then?

16 A I believe we focused on Redmond 74 to start  
17 with. He was looking at acquiring the entire Redmond  
18 74 project, which would have contemplated signing up  
19 for about a \$24 million bank loan commitment.

20 Q And was that something he would capable of  
21 doing, according to him?

22 A I believe so, yes.

23 Q And so is that the way the deal went?

24 A That's the way the deal was documented, yes.

25 Q And then what happened?

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1 taken out of the deal, right? They would have been  
2 paid off?

3 A I believe so, yes.

4 Q So the proposal currently before the  
5 bankruptcy court doesn't have Rainier Capital being  
6 paid off, except way down the line, potentially as  
7 part of some plan?

8 A I believe they get periodic payments every  
9 time units are taken down.

10 Q What are those periodic payments, if you  
11 know?

12 A The numbers have changed, but I think  
13 currently they are about \$16,000 per unit.

14 Q Is the reason for this bankruptcy that you  
15 needed to get Rainier Capital and its loan documents  
16 out of the way?

17 A No, the reason for the bankruptcy is to allow  
18 us to go forward with the sale of the project.

19 Q You said you couldn't build out the project  
20 without the bankruptcy?

21 A No, I said we could not build out the project  
22 without obtaining vertical financing on the loans,  
23 and Rainier Capital has refused to subordinate the  
24 vertical financing.

25 Q Were there alternatives available to you

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1 the marketing name the same as the name of the LLC.

2 Q And did somebody tell Mr. Housley, you know,  
3 we want the -- the buyer ought to have that name,  
4 Velo, in it?

5 A I believe so.

6 Q Who would that be?

7 A That would have been Mr. Baldwin or myself.

8 Q What do you recall about at that, if it was  
9 you?

10 A I probably gave them a marketing brochure or  
11 a write-up on it that had the name Velo in it. It  
12 could be that simple, or our attorneys may have  
13 contacted Mr. Johnston when they documented the name.

14 Q Have your attorneys -- and I'm not asking  
15 about any communications with your attorneys, I am  
16 asking whether your attorneys have prepared any  
17 documents related to the formation of Velo Redmond,  
18 LLC.

19 A I have no knowledge of that.

20 Q Take a look at the second page.

21 A (Complies.)

22 Q The third bullet point confirms that under  
23 this proposal, Rainier Capital Group would be paid  
24 2.9 million, right?

25 A Yes.

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1       this risk to develop the projects to obtain the  
2       management fee and not have the profit potential in  
3       the real estate, doesn't excite anybody that much.

4           Q     So why did they do it?

5           A     Do what?

6           Q     Why did they position themselves to continue  
7       to receive development fees and construction fees  
8       without keeping any of the upside for developing?

9                   MR. KORNFELD: I'm assuming you are  
10      talking about the Velo deal that's on the table?

11                  MR. WEATHERHEAD: Yes.

12                A     Well, as we have discussed previously, the  
13      Velo deal is stalled at this point. We don't have  
14      opportunities to start vertical on the project,  
15      because Rainier Capital has stated that they will not  
16      fully subordinate to HomeStreet loans -- HomeStreet  
17      Bank loans. This real estate market, you cannot  
18      obtain external financing for construction of the  
19      project unless that bank is also on the land portion,  
20      it's just simply not happening. You can read any  
21      newspaper you want to and you will see how banks are  
22      retrenching and trying to dump their real estate.

23                  Our only choice for financing for the Velo  
24      deal is either through a total outside source and  
25      sale of the project or through HomeStreet Bank.

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1 name of the firm.

2 Q Where is he officed?

3 A Mercer Island.

4 MR. WEATHERHEAD: If you will give me  
5 about five minutes to chat here. I think we are  
6 done.

7 (A brief recess.)

8 Q Last night we were furnished with a CD-ROM  
9 with about 35,000 pages of documents on it. Are you  
10 familiar with what I'm talking about?

11 A Yeah.

12 MR. KORNFELD: I'll tell you that it's  
13 47,000.

14 MR. WEATHERHEAD: I only got to 35,000  
15 before I got sleepy.

16 Q Can you tell me what's on that disk?

17 A I believe there are two major files on it.  
18 One is for Redmond, one is for Little Boat North.  
19 There were subfiles, one having to do with the  
20 acquisition of the property, (inaudible) packages.  
21 There could be purchase and sale agreements on that,  
22 things of that nature.

23 The other side is a financial drive copied  
24 off of our system. It has all the pro formas that  
25 have ever been created for the project, whether they

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Robert F. Pascal

Page 1

UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF WASHINGTON

In re	)
LITTLE BOAT NORTH, INC.	)
7525 SE 24th STREET, #650	)
MERCER ISLAND, WA 98040,	)
Tax ID 20-3046005,	)
Debtor.	)
	(Administratively
	Consolidated with
	Case No. 08-15825)
In re	)
REDMOND 74, INC.	)
7525 SE 24TH STREET, #650	)
MERCER ISLAND, WA 98040,	)
Tax ID 20-5820789,	)
Debtor.	)

DEPOSITION UPON ORAL EXAMINATION

OF

ROBERT F. PASCAL

Taken at 1201 Third Avenue

Seattle, Washington

DATE TAKEN: OCTOBER 14, 2008  
REPORTED BY: SHERRILYN SMITH, CCR# 2097

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Robert F. Pascal

Page 11

1 Q And it's also in bankruptcy?

2 A Yes.

3 Q Prior to bankruptcy were the loans in  
4 default?

5 A We had not declared a default. Technically,  
6 they may have been in default. Usually, the key is  
7 when we declare a default, but we hadn't declared  
8 one.

9 Q So it's possible that if you had reviewed the  
10 file with an eye toward determining whether there was  
11 a default, you might have concluded that there was  
12 one, but you made a discretionary decision not to do  
13 so?

14 MR. CAHN: Objection. Calls for  
15 speculation. Misstates prior testimony.

16 Q You can answer.

17 MR. CAHN: You can answer.

18 A Would you say that again?

19 Q Sure. Had you made a discretionary decision  
20 not to declare a default prior to the bankruptcy?

21 A We had not -- we had not made any particular  
22 decision regarding a default. It's not my decision  
23 to make.

24 Q Whose decision is it?

25 A It would typically be an underwriting

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Robert F. Pascal

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1 talk about that you recall as being issues of  
2 importance to the bank, without telling me, you know,  
3 I told him that our lawyers said this or our lawyers'  
4 judgment about the risk was that?

5 It may not be possible to answer the question  
6 the way I posed it, but if you can, that's what I'm  
7 asking for.

8 A Our conversations really discussed whether or  
9 not there -- you know, legally this was something  
10 that would -- that could be done.

11 Q Okay.

12 Did you talk to Mr. Todhunter or anybody else  
13 at the bank about developing a Plan B in the event  
14 that Rainier proved to be right, that this was not an  
15 arm's length transaction?

16 A Well, our original plan was to have The  
17 Dwelling Company build this on their own with Rainier  
18 Capital as a subordinate lender. That was always the  
19 original plan. Because of the fact that Rainier  
20 Capital was in a subordinate position, it would not  
21 be subordinate and would not take payment of their  
22 principal and interest. We didn't really see an  
23 alternative other than selling the land.

24 Q What caused you to think that Rainier  
25 wouldn't accept payment of its principal and

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Robert F. Pascal

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1 interest?

2 A Well, maybe I misspoke. I don't know that  
3 we -- we knew that they would not accept payment of  
4 principal and interest. I think it was more that  
5 there probably was not room in the transaction to pay  
6 everybody; that is, without us assuming an equity  
7 position.

8 Q Or taking a position for future advances  
9 subordinate to Rainier Capital?

10 A Or loaning well outside our normal  
11 guidelines.

12 Q Or requiring the founders to step up and put  
13 more equity into the program?

14 A If they could pay off Rainier, that would be  
15 something that could work, but apparently they were  
16 unable to do that.

17 Q Point of fact, didn't you suggest to  
18 Mr. Wordstrom --

19 MR. WEATHERHEAD: Did I get that right?

20 MR. KORNFELD: Stromswold.

21 MR. WEATHERHEAD: I knew I said it  
22 wrong.

23 Q Did you suggest to Mr. Stromswold that the  
24 bank would make an advance to pay off Rainier  
25 Capital, leaving Rainier Capital to await the end of

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Robert F. Pascal

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1 A Okay.

2 Q After approval of the June 6, 2008 request,  
3 how did it come up that this interest loan and this  
4 attorneys fee loans were going to be necessary to  
5 permit the founders to go forward?

6 A Well, we had issued our commitments in  
7 documents on both loans and requested the  
8 subordinations be signed and Rainier Capital refused  
9 to sign them.

10 Q And then what?

11 A Well, then the borrower felt that the only  
12 alternative was to either go into state court or go  
13 into bankruptcy and get a decision as to whether the  
14 project can go forward or not.

15 Q More specifically, a decision as to whether  
16 Rainier was obliged by its documents to subordinate?

17 A Yes.

18 Q And without involving any discussions you may  
19 have had with your counsel, were you told why the  
20 option to go to state court was not taken?

21 A I -- I can't really answer that without  
22 thinking of what our counsel was telling me.

23 Q Did you talk to Mr. Baldwin about that?

24 A I'm sure I did.

25 Q Do you remember what he said about the

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